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FEDERAL COMMUNICATIONS COMMISSION
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20054

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

REPLY COMMENTS OF MFS COMMUNICATIONS COMPANY, INC.

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Dated: January 10, 1997

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SUMMARY

- ***Competitive Neutrality***. MFS and many other parties support the Joint Board's recommendation to add competitive neutrality to the Commission's universal service policy principles.
- ***Access to Advanced Services***. MFS recommends that the Commission promote access to advanced services by adopting the network modernization standards required of rural telephone companies under the provisions of the Rural Electrification Loan Restructuring Act of 1993 ("RELRA"). Among other things, the RELRA requires plans to deploy networks capable of 1 megabit transmission speeds. The RELRA network modernization standards have been implemented in Rural Utility Service ("RUS") rules and plans developed by the majority of states including many with substantial rural, high-cost service areas. Since Congress requires compliance with RELRA standards as a prerequisite for receipt of federally subsidized telephone loans, the same standards should be a prerequisite for receipt of federal universal service funds. Applying such standards is consistent with the practices of state commissions that tie regulatory relief and other incentives to network modernization, and consistent with the comments of the RUS which recommended linking the level of universal service support to a carrier's infrastructure investment.
- ***Universal Service Support Should be Explicitly Reflected on Customers' Bills***. MFS and many commentors suggested that universal service support be explicitly reflected on customers bills to meet the requirements of §254(e). The Commission

should reject the Joint Board's conclusion that end-user surcharges should not be used to recover universal service funding.

- ***Ensuring Affordable Rates Should not be Confused with Incumbent Carriers' Financial Interests***. The Commission should develop universal service support mechanisms that focus on providing support to customers, not carriers. Support should be narrowly targeted to low income customers, customers living in high-cost service areas, schools, libraries and rural health care providers. Support should not be designed to recoup competitive losses or ensure recovery of investments.
- ***Carriers Eligible for Universal Service Support***. Any carrier that meets the minimum network standards and actually provides service to eligible low income customers, customers who live in high cost areas, eligible schools, libraries or rural health care providers should be eligible to receive the subsidies that attach to such customers irrespective of the technologies or service configuration used by the carrier or whether the carrier is an incumbent or a new entrant.
- ***Proxy Cost Models Should be Generally Independent of Incumbent Carriers' Costs***. Some parties complained that proxy cost models were flawed because they failed to reflect the incumbent carriers' costs. Proxy costs should not generally reflect the incumbent carriers' costs, but rather, provide an estimate of the costs of providing service in a competitive market -- the forward-looking costs that an efficient new entrant would face. However, proxy costs should be no higher than the incumbent's embedded costs (a new entrant would not enter a market if its costs were higher than the incumbent), and if universal service support is based on forward-looking technologies, a recipient's network should be capable of supporting such technologies as a prerequisite to receipt of universal service funds based on forward-looking costs.

- ***High-Cost Support Should be Based on Costs, Not Average Revenues.*** MFS and other commentors argued that costs rather than average revenues should be used as a universal service benchmark. In a competitive market, average revenues can be expected to decline, which would increase universal service support under the formula proposed by the Joint Board.
- ***Universal Service Support Should not be Extended to Inside Wiring***. MFS and many other commentors argued that universal service support for schools and libraries should extend only to telecommunications services, which do not include inside wiring.
- ***Nine-Digit Zip Codes Should be Used to Target Support to Low Income Households and High-Cost Areas***. MFS proposes that the Commission use nine-digit zip codes as a mechanism to uniquely identify customers eligible for low income or high-cost support.
- ***Contributions to Universal Service Should be Based on Total (Interstate and Intrastate) Revenues less Payments to Telecommunications Carriers***. The Commission should adopt the Joint Board's recommendation that contributions to universal service funding be based on carriers' total telecommunications revenues less payments to other telecommunications carriers.

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INTRODUCTION

MFS Communications Company, Inc. ("MFS") submits these reply comments in response to the Joint Board's Recommended Decision issued on November 8, 1996.[1/] MFS's reply comments generally follow the outline of the Joint Board's Recommended Decision and the comments MFS filed in the above captioned proceeding.

I. PRINCIPLES

A. Definition of Competitive Neutrality

MFS supports the Joint Board's recommendation that competitive neutrality be included among the Commission's universal service policy principles.[2/] Developing universal

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1/ In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, FCC 96J-3, Recommended Decision, released Nov. 8, 1996 (hereafter cited as "Recommended Decision").

2/ Recommendation Decision at ¶ 23.

service policies and mechanisms that are competitively neutral is consistent with the pro-competition intent of the Telecommunications Act. In its comments, MFS suggested a definition of competitive neutrality.[3/]

There was broad agreement that application of universal service mechanisms should be competitively neutral and general agreement that competitive neutrality means that application of universal service mechanisms should not disadvantage any competitor. [4/] Southwestern Bell suggested a definition of competitive neutrality that was similar to MFS's suggested definition.[5/] The California Department of Consumer Affairs suggested that competitive neutrality should be viewed from a customer rather than an industry perspective and suggested that all customers share equally in supporting universal service.[6/]

Based on the pro-competition intent of the Telecommunications Act and the consensus of commentors at all ends of the competitive spectrum, MFS urges the Commission to incorporate competitive neutrality into its universal service principles. Since some parties improperly view universal service as a "make whole" mechanism, MFS urges the Commission

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3/ MFS at pg. 2. "Subject to requirements established by the Commission that all firms or technologies meet certain minimum standards, a mechanism or rule is competitively neutral when its application does not give any firm a price, cost or other economic advantage or disadvantage relative to competing firms or technologies. A competitively neutral mechanism or rule is not designed to guarantee revenues or ensure that firms recover their investments or costs."

4/ See, *e.g.*, GTE at pp. 11-12; BellSouth at pp. 9-18; NYNEX at pg. 4; MCI at pg. 1; AT&T at pg. 2; and ALLTEL at pg. 4.

5/ Southwestern Bell at pg. 6. "Universal service support mechanisms and rules should be applied in a manner which neither advantages nor disadvantages one provider of telecommunications service over another, nor favors or disfavors one technology over another."

6/ California Department of Consumer Affairs at pg. 21.

to explicitly recognize that a competitively neutral mechanism or rule is not designed to guarantee recovery of investment nor designed to assure a particular level of revenues.

B. The Joint Board's Recommended Decision Inadequately Addresses Access to Advanced Services

In its comments,[7] MFS argued that the Joint Board's Recommended Decision failed to adequately promote access to advanced telecommunications and information services in all regions of the Nation -- a universal service policy principle that is specifically listed in §254(b),[8] and a policy goal featured prominently throughout the Telecommunications Act.[9] To promote access to advanced telecommunications and information services as required by §254(b)(2), MFS suggested [10] that the Commission adopt the network modernization standards mandated by Congress for rural telephone companies in the Rural Electrification Loan Restructuring Act of 1993 ("RELRA").[11] The RELRA requires state or territorial public

7/ MFS at pp. 3-12.

8/ 47 U.S.C. §254(b)(2). "Access to advanced telecommunications and information services should be provided in all regions of the Nation."

9/ 47 U.S.C. §§ 254(b)(2) (access to advanced services), (b)(3) (rural access to advanced services), (b)(6) (access to advanced services for schools, health care providers and libraries), (h)(2) (advanced services for schools, health care providers and libraries), and, 706 (regulators shall encourage the deployment of advanced telecommunications capabilities).

10/ MFS's recommendation is also described in its Reply Comments at pp. 12-18 (filed May 7, 1996), the comments it filed in response to two subsequent requests for information filed with the Joint Board and the Commission on August 2, 1996 (pp. 11-28) and August 9, 1996 (pp. 3-5), and in a written *ex parte* filed with the Commission and members of the Joint Board on October 17, 1996.

11/ 107 Stat. 1356, codified in 7 U.S.C. § 935 (1994).

utility commissions or borrowers to develop network modernization plans as a prerequisite for otherwise eligible carriers to receive federally subsidized loans for telecommunications utilities.[12] Application of the statutory network modernization standard is clearly feasible since the Rural Utilities Service ("RUS") has promulgated rules implementing the above statute[13] and implementation plans from the majority of states and territories (many with substantial rural, high-cost and/or low-income populations) have been filed with and approved by the RUS.[14] If Congress set these minimum standards for rural telephone companies as a prerequisite for receipt of federal subsidies, they should also be the minimum standard for all local telecommunications providers as a prerequisite for federal universal service subsidies,

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12/ The Act specifically requires that
"a telecommunications modernization plan must, at a minimum, meet the following objectives:
(i) The plan must provide for the elimination of party service.
(ii) The plan must provide for the availability of telecommunications services for improved business, educational, and medical services.
(iii) The plan must encourage and improve computer networks and information highways for subscribers in rural areas.
(iv) The plan must provide for --
(I) subscribers in rural areas to be able to receive through telephone lines --
(aa) conference calling;
(bb) video images; and,
(cc) data at a rate of at least 1,000,000 bits of information per second; and,
(II) the proper routing of information to subscribers."

7 U.S.C. §935(d)(3)(B). [emphasis added]

13/ 7 C.F.R. §1751.106 *et seq.*

14/ MFS's Attachment 1, filed with its Comments, shows the status of plans filed with the RUS.

absent a showing of technical infeasiblity.[15] MFS is not suggesting that high-capacity services or deployment of broadband networks be subsidized by universal service funds; it is merely suggesting that networks be capable of at least the same transmission speeds that Congress requires of rural telephone borrowers. By making such capabilities a prerequisite for receipt of universal service funds, the Commission will encourage the deployment and access to advanced telecommunications and information services as required by §254(b)(2).

MFS's proposal is consistent with the incentives often provided by state regulators. For example, the Delaware Public Service Commission indicated that it granted Bell Atlantic price regulation in exchange for a commitment to make a $250 million investment to make its network capable of digital transmission and make every switch ISDN capable.[16] It is common practice for state regulators to tie various types of regulatory relief or other financial incentives to network modernization. The Commission should follow state commissions' examples and tie receipt of universal service funds to network modernization.

MFS's proposal is also consistent with RUS's suggestion. RUS advocated that the level of universal service support should be related to a carrier's infrastructure investment.

> RUS believes that a relationship should be established between the amount of USS [Universal Service Support] provided to an eligible telecommunications carrier and the amount of investment the carrier makes in infrastructure. If the carrier fails to maintain certain investment levels, the USS could be reduced to a level corresponding to actual investment, or additional investment at some

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15/ For example, a wireless carrier might not be able to develop a network capable of 1Mb/second transmission speeds simply because it cannot obtain sufficient spectrum due to limited spectrum and regulations governing allocation of spectrum. In such instances, where a carrier cannot conform with the requirements due to factors beyond its control, the minimum network standards should be waived.

16/ Chairman of the Delaware Public Service Commission at pg. 3.

> level could be required. The percentage mentioned above could even be a variable set by the states or the USS Administrator in consideration of the quality and reliability of service the carrier provides.[17]

MFS believes that there should be a competitively neutral relationship between universal service and infrastructure investment. To establish such a linkage, the Commission can either establish minimum network standards, such as the RELRA standard mandated by Congress, or it can develop an explicit linkage between the level of universal and infrastructure investment, as suggested by the RUS. However, the linkage should also be competitively neutral. Mechanisms that limit universal service support to only facilities-based carriers or only carriers that commit to carrier of last resort obligations are infrastructure-related proposals designed to restrict universal service subsidies to incumbent carriers and are obviously not competitively neutral.

C. Universal Service Support Received and Paid for Should be Explicitly Reflected on Customers' Bills

In its comments, MFS argues that the mechanisms proposed by the Joint Board do not ensure that universal service support will be explicit as required by §254(e).[18] MFS argued that there are two aspects of making universal service explicit -- those who receive support should know how much support they receive and those who provide support should know how much support they are providing. MFS recommended that customers' bills explicitly reflect the universal service support they provide as well as the support they receive. In contrast,

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[17] RUS at pg. 3.

[18] 47 U.S.C. §254(e) requires that "[a]ny such support should be <u>explicit</u> and sufficient to achieve the purposes of this section."

the Joint Board rejected suggestions that universal service support be funded through an end-user surcharge, arguing that carriers and not customers should provide universal service support.[19] Thus, the Joint Board does not acknowledge that customers will ultimately pay for any universal service obligations placed on carriers, and does not recommend that the universal service support provided by customers be an explicit component of their bill.

MFS and a broad cross-section of commentors disagree with the Joint Board's analysis and recommendation that universal service support not be explicitly reflected on end-users' bills. In his affidavit, Dr. Crandall, for example, argues that "most of the burden of these charges will be borne by telecommunications users, not by the carriers themselves, since these contributions are essentially taxes on telecom services that will be passed on to final consumers of the services."[20] Several commentors recommended that universal service costs be recovered through an explicit surcharge on customers' bills.[21] In also recommending an end-user surcharge, the California Public Utilities Commission observed that retail surcharges are a competitively neutral means of collecting universal service funds and that such surcharges eliminate the problem of generating revenues from cost-based unbundled network elements.[22]

19/ Recommended Decision at ¶ 812.

20/ Bell Atlantic, Affidavit of Robert Crandall, pg. 2.

21/ See, *e.g.*, Rural Telephone Coalition at pp. 35-36; Ameritech at pp. 30-31; BellSouth at pp. 14-16; NYNEX at pg. 23; California Public Utilities Commission at pg. 13; Pacific Telesis at pp. 20-21; USTA at pg. 22; US WEST at pp. 45-46; Sprint at pg. 10; Southwestern Bell at pp. 11, 13; CompTel at pg. 14; LCI at pg. 14; and, Bell Atlantic at pg. 8.

22/ California Public Utilities Commission at pg. 13.

MFS recommends that the Commission recognize the comments of parties in this proceeding and require that universal service contributions and payments be explicitly reflected on customers' bills. Because prices reflect costs in a competitive market, customers will ultimately pay for any universal service obligations imposed on telecommunications carriers. Those costs ought to be honestly, explicitly reflected on customers' bills rather than hidden in rates. Telecommunications consumers should know how much support they are providing to subsidize service to low income customers, high-cost service areas, schools, libraries, and rural health care providers. The requirement of §254(e) that "*[a]ny such support should be explicit*" seems to mandate such an explicit disclosure.

II. AFFORDABILITY

A. Ensuring Affordable Rates Should not be Confused with Incumbent Carriers' Financial Interests

Some commentors confuse maintaining affordable rates with assuring recovery of incumbent carriers' investments and/or guaranteeing incumbent carriers' revenues or profits. For example, while they advocated that universal service mechanisms should be competitively neutral, many incumbent carriers argued that universal service mechanisms should ensure recovery of investments and embedded costs.[23/] USTA argues that explicit and implicit subsidies in incumbent carriers' rates amount to $21 billion annually, implying that any

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[23/] See, *e.g.*, BellSouth at pp. 6-7 (proxy cost models should recognize and include embedded costs that incumbent carriers have a constitutional right to recover); GTE at pg. 31; Rural Telephone Coalition at pp. 4-10 (proxy cost models should reflect the actual costs of rural telephone companies); Pacific Telesis at pg. 6; and, Southwestern Bell at pg. 23-31 (proxy cost models must replicate actual costs).

universal service support program must ensure that incumbent carriers continue to realize these revenues in a competitive market.[24] Absolutely none of the explicit universal service policy principles included in §254 require or imply that universal service should be designed to maintain incumbent carriers' revenues or profits or ensure recovery of incumbent carriers' investment in a competitive environment. The Commission should reject disingenuous schemes designed to shelter incumbents from competition and focus instead on developing narrowly targeted mechanisms to assure affordable rates for low income customers, customers living in high-cost areas, schools, libraries and rural health care providers. Said differently, universal service should focus on supporting customers, not carriers.

In a competitive market, no firm is guaranteed recovery of its investment. Firms invest and build facilities in anticipation that they will be able to offer services demanded by consumers in sufficient volumes to realize a profit. Certainly, new market entrants, like MFS, are building facilities with no guarantee that they will earn revenues sufficient to recover their investment. Obviously, it would not be competitively neutral to develop universal service mechanisms that assured incumbents recovery of their investments.[25]

Some incumbent carriers argued that universal service mechanisms, such as the application of a proxy cost model to determine high-cost recovery, should be sufficient to allow

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24/ USTA at pp. 4-9.

25/ Given AT&T's experience with competition in the long distance market and the fact that its revenues are earnings are at record levels in spite of losing more than 25% of the market and decreasing average prices more than 40%, competition probably will not harm incumbent carriers that learn to compete. Thus, even if the incumbent carriers' arguments were correct that universal service should be used to recoup competitive losses, it is not clear that there necessarily would be any losses to recoup or any failure of incumbent carriers to recover their investment.

recovery of embedded costs, and that failure to allow recovery of embedded costs is an impermissible taking. For example, while it supports the use of a proxy cost model, US WEST argued that any universal service mechanism must assure total recovery of the capital investment -- both new and embedded -- associated with providing universal service.[26] US WEST proposes that new construction of high-cost facilities be subsidized through the universal service fund, and that investment in existing high-cost facilities be amortized and recovered over a short (5 years) period, presumably by universal service funds. However, it also recommends that new entrants should not receive any universal service funding for duplicative facilities.[27] US WEST's proposal is intended to ensure that incumbent carriers will recover their investment in facilities in high-cost areas, but deny similar recovery for their competitors. The Commission should reject such competitively biased schemes.

Moreover, US WEST's universal service proposal is flawed because it confuses the rates paid by consumers with the investment made by carriers. Universal service support should not be designed to recover carriers' investments in high-cost areas, but to assure that the rates paid by customers who live in high-cost areas are affordable. As MFS proposes, universal service support should attach to the customer and be reflected on a customer's bill so that a carrier would receive universal service support only for the high-cost customers it actually serves. Thus, a carrier might build a network to a high-cost area but receive no high-cost support if it fails to attract customers. US WEST's proposal has the wrong focus; its focus is not on assuring affordable rates, but on assuring US WEST's recovery of investment.

26/ US WEST at pp. 8-15.

27/ US WEST at pg. 13.

MFS strongly recommends that universal service be targeted to customers (low income customers or customers living in high-cost areas) rather than carriers, and carriers would realize universal service support only by providing service to supported customers.

In its comments, GTE describes the potential for arbitrage that arises if rates are maintained at geographically averaged levels.[28/] It recommends that universal service support be provided only to carriers that commit to carrier of last resort obligations and to maintain the same geographically averaged rates as the incumbent. GTE reasons that these requirements are necessary to prevent new entrants from focusing on the consumers with the lowest costs and leaving the incumbent with a network that serves only high-cost areas. Again, GTE's focus is on ensuring recovery of a carrier's investment in infrastructure rather than on the rates paid by consumers, and GTE's proposal would obviously restrict entry into many markets in order to ensure recovery of its investment. MFS proposes that carriers be allowed to geographically deaverage their rates, so that customers who live in high-cost areas could receive a bill that reflects the actual costs of providing service to their area. To ensure that the rates paid by customers remain affordable, MFS proposes that such customers receive an explicit high-cost credit that they could apply (in the form of a credit on their bill) to whomever or whatever service they selected.[29/] If the Commission allows geographic deaveraging,

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28/ GTE at pp. 14-17.

29/ A customer could select a service that is more expensive than basic local service. Likewise, carriers could offer deaveraged cost-based rates, geographically averaged rates, or below-cost rates as dictated by the market. A customer's credit would be the same irrespective of who or what type of service is selected.

GTE's concern about cream skimming low-cost customers is eliminated and the Commission would not have to resort to mechanisms that limit competition.

While the Commission has ordered geographic deaveraging of unbundled local loop rates,[30] it may not have the authority to require geographically deaveraged local service prices. However, the Commission can and should make receipt of federal universal service funds contingent on states allowing geographically deaveraged rates. Thus, for example, if Missouri prohibited geographic deaveraging of local service rates, then no carrier -- incumbents or new entrants -- would be eligible to receive federal high-cost universal service support for customers served in Missouri.

III. CARRIERS ELIGIBLE FOR UNIVERSAL SERVICE SUPPORT

Any carrier that meets the minimum network standards described above and actually provides supported service to low income customers or to customers who live in high-cost service areas, or provides supported services to eligible schools, libraries or health care providers should be eligible for the universal service support that attaches to its customers. The Joint Board's Recommended Decision and many of the commentors generally embraced this principle, but some argued that "eligible telecommunications provider" should be interpreted to exclude resellers or to limit support based on the proportion of facilities actually provided by a carrier.[31] In its comments, MFS suggested that §214(e)(1), which defines an

[30] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket 96-98, ¶¶ 764-766 (released Aug. 1, 1996).

[31] See, *e.g.*, Pacific Telesis at pp. 24-26; Southwestern Bell at pp. 21-22; and US WEST (continued...)

eligible carrier, should be interpreted broadly. Under §214(e)(1), an eligible carrier is a carrier that offers services "either using its own facilities or a combination of its own facilities and resale of another carrier's services." The Joint Board interprets this to exclude a "pure" reseller because that is not a "combination" of facilities and resale of another carrier's services. An alternative interpretation, that MFS believes is consistent with the policy rationale of the Telecommunications Act, would include resellers, even pure resellers, in the definition of eligible telecommunications carriers.[32/]

Arguments about the extent to which various carriers are eligible for universal service support vanish if universal service support is focused on assuring affordable rates and not on assuring recovery of carriers' investments. That is, if the Commission adopts MFS's proposal to explicitly reflect low income and high-cost credits on customers' bills irrespective of who serves the customer, it need not agonize over whether the carrier's provision of service is a "combination of its own facilities and resale of another carrier's services." Under MFS's proposal, universal service support would depend on the customer's characteristics and not

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31/ (...continued)
at pp. 12-13.

32/ A combination could be liberally interpreted to include *de minimis* use of a carrier's facilities. There is no debate that resellers could serve low income customers or high-cost areas. Why would Congress want to subsidize low income customers and high-cost areas, but prohibit an entire class of competitors from providing such subsidized services? The policy purpose of §214(e)(1) might have been to create a mechanism to ensure that there was no double recovery of universal service subsidies. That is, Congress may have created the definition of an eligible telecommunications carrier to prevent both the facilities-based carrier and those who resell those facilities from receiving subsidies for the same service.

the carrier's.[33/] Also, under MFS's proposal, customers would have a richer choice of carriers, and the pro-competition intent of the Telecommunications Act would be promoted.

Some parties argued that receiving universal service support should be contingent on a carrier assuming carrier of last resort obligations.[34/] If support is targeted to customers rather than carriers, the Commission would not have to become mired in determining whether a carrier served as a carrier of last resort. Moreover, a requirement that only the carrier of last resort (especially if there is only one carrier of last resort) is eligible for universal service subsidies is not competitively neutral as it could create a cost disadvantage for a substantial number of carriers that otherwise could provide services to low income customers, customers living in high cost areas, schools, libraries and rural health care providers.

IV. HIGH COST SUPPORT

A. Proxy Cost Models Should be Generally Independent of Incumbent Carriers' Costs

Some parties were opposed to using proxy cost models to apportion or determine high cost support because such models do not reflect the incumbent carriers' embedded costs.[35/]

33/ As described in its comments and below, MFS's proposal to use nine-digit zip codes to apportion universal service support eliminates the potential that both pure resellers and end-users receive high-cost support for the same service. Only one high-cost (or low income) credit should be available to the customer.

34/ See, *e.g.*, Ameritech at pp. 8-10 (carriers that receive universal service support should be required to assume carrier of last resort obligations).

35/ See, *e.g.*, BellSouth at pp. 6-7 (proxy cost models should recognize and include incumbent carriers' embedded costs); Pacific Telesis at pp. 12-13 (high cost fund size should be based on actual costs of the incumbent carrier, and a proxy cost model
(continued...)

These critics of proxy cost models generally miss the point. Proxy costs models should not reflect the costs of the incumbent carrier, but should reflect "[t]hose costs [that] best approximate the costs that would be incurred by an efficient competitor entering that market."[36/] The intent of using proxy costs is not to estimate the incumbent carrier's costs, but to estimate the costs of providing service in a competitive market. Thus, proxy costs are the forward-looking costs that a new entrant would face, and not necessarily the incumbent's actual costs, technologies and network deployment.

However, the incumbent carrier's costs are relevant to the determination of forward-looking costs in two ways. First, in a competitive market, a competitor would not enter a market unless its forward-looking costs for comparable services were lower than or equal to the incumbent carrier's costs. Thus, if proxy costs are intended to reflect the costs of an efficient market entrant, they can be no higher than the incumbent's embedded costs.[37/] Second, if an incumbent carrier receives compensation from the universal service fund based on forward-looking costs and technologies, then the incumbent's network ought to be capable of actually providing the forward-looking technologies reflected in the forward-looking costs that form the basis of the universal service support it receives.

35/ (...continued)
should determine how to distribute those actual costs); USTA at pp. 12-15; and, Southwestern Bell at pp. 23-31.

36/ Recommended Decision at ¶270.

37/ See comments of Washington Utilities and Transportation Commission at pg. 4 for a similar argument that proxy cost models should yield cost estimates less than or equal to the book costs of serving exchange areas.

B. High-Cost Support Should be Based on Costs, Not Average Revenues

The Joint Board recommends that high cost support be based on the difference between a benchmark figure and the proxy costs for a specific area, such as the proxy costs for a specific census block. The Joint Board recommended that the benchmark be based on the national average revenues per line, where revenues include local service, discretionary and access services. The Joint Board recommended using a measure of total revenues per line as the benchmark in recognition that a loop supports a variety of services and generates a variety of revenues.[38/]

In its comments, MFS recommended that the benchmark be based on a national average proxy cost rather than average revenues because competition can be expected to reduce the average revenues per line and expand rather than reduce reliance on universal service funding.[39/] Likewise, the California Public Utilities Commission argued that competition would make a revenue benchmark unstable, and urged that a cost-based benchmark be developed.[40/] The Texas Public Utility Commission also questioned how price reductions, particularly access price reductions, would affect the size of the universal service fund.[41/] Clearly, as the market becomes more competitive, reliance on competition distorting subsidies should be reduced, not increased.

38/ Recommended Decision at ¶¶ 309-317.

39/ MFS at pp. 24-26.

40/ California Public Utilities Commission at pg. 6.

41/ Texas Public Utility Commission at pp. 6-7.

V. SUPPORT FOR SCHOOLS AND LIBRARIES AND HEALTH CARE PROVIDERS

A. Universal Service Support for Inside Wiring and Items that are not Telecommunications Services is not Authorized by the Telecommunications Act

The Joint Board recommends including inside wiring among the subsidized services provided to schools and libraries.[42/] In its comments, MFS argued that inside wiring is not a telecommunications service, and providing universal service support for schools, libraries and health care providers is clearly limited to support for telecommunications services. Most commentors agreed with MFS that universal service support for inside wiring is beyond the scope of the Telecommunications Act and the Commission's jurisdiction.[43/] AT&T argued that subsidizing inside wiring and enhanced services would be improper as it would require telecommunications carriers to subsidize the operations and activities of non-telecommunications providers who are not required to contribute to the universal service fund.[44/] The Commission should not adopt the Joint Board's recommendation to subsidize the provision inside wiring.

42/ Recommended Decision at ¶¶ 458-465, 473-484. Internal connections are defined to include traditional inside wiring, routers, hubs, network file servers, and wireless LANs, but <u>exclude</u> personal computers

43/ See, *e.g.*, Ameritech at pp. 18-19; NYNEX at pp. 40-41; BellSouth at pp. 25-28; North Dakota Public Service Commission at pg. 3; Illinois Commerce Commission at pg. 2; California Public Utilities Commission at pp. 23-30; ALLTEL at pg. 5; GTE at pp. 89-96; Pacific Telesis at pg. 37, 46; USTA at pg. 34; Sprint at pp. 12-13; Bell Atlantic at pp. 20-21; and Southwestern Bell at pp. 43-44.

44/ AT&T at pp. 18, 20.

VI. Administration

A. Nine-Digit Zip Codes Can be Used to Target Support to Low Income Households and High-Cost Service Areas

In its comments, MFS recommended using the nine-digit zip codes that appear on customers' bills as a practical mechanism for managing customers entitled to high-cost and low income support. The universal service administrator would maintain a database of nine-digit zip codes with fields that indicate the local carrier chosen by the customer, whether the customer at that location is entitled to low income support, high-cost support, and whether a support payment has been generated for a particular month. Carriers would identify which customers are entitled to support and would seek reimbursement for providing supported service (to low income customers or high-cost areas) would simply submit a list of nine-digit zip codes of potentially qualifying customers' nine-digit zip codes (or all of their customers' nine-digit zip codes) to the administrator, which would match the list against the master database to determine the appropriate payment owed to the carrier. Alternatively, the universal service administrator, using information from proxy cost models and income data from various social service agencies, could generate a listing -- by nine-digit zip code -- to match against carriers' billing records indicating the type of assistance appropriate for individual households. Carriers would then explicitly reflect any universal service support on the bills they render to customers. Under MFS's proposal, the nine-digit zip codes would reflect the characteristics of the customer's <u>billing</u> address and only one high-cost or low-income payment would be made for any nine-digit zip code.[45] Thus, support for second lines, support for vacation homes, and duplicative support for services provided by competing carriers would be eliminated.

MFS believes that its proposal addresses the concerns raised by parties that it would be administratively impossible to identify and limit support to a single line in the primary residence or business.[46] MFS's proposal also focuses support on low income and high-cost customers and not carriers. MFS urges the Commission to adopt its nine digit zip code proposal.

B. Contributions to Universal Service Should be Based on Total (Interstate and Intrastate) Revenues less Payments to Telecommunications Carriers

The Joint Board recommended that contributions to support universal service should be based on a carrier's gross telecommunications revenues net of payments to other carriers.[47] MFS supports this recommendation with the clarifications that the base include only the revenues that a firm earns by providing telecommunications services, and that total telecommunications revenues -- both interstate and intrastate -- should be included in the calculation. The universal service policies of the Telecommunications Act are intended to

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45/ There may be some instances where more than one household shares the same nine-digit zip code, such as cases where the zip code segment is for a single floor of an apartment building. The nine-digit zip code could be augmented (*e.g.*, adding a letter or another digit) to convert the zip code to uniquely identify households.

46/ See, *e.g.*, Southwestern Bell at pg. 37 (limiting support to primary residence line would be practically impossible to administer); USTA at pg. 30; US WEST at pg. 25; and, Pacific Telesis at pg. 19.

47/ Recommended Decision at ¶ 807.

encourage end-users to subscribe to telephone service in toto, not just interstate or intrastate telecommunications.

NYNEX's comments[48] dramatically illustrate the impacts of including various types of revenues.

UNIVERSAL SERVICE CONTRIBUTIONS BASED ON INTERSTATE AND INTRASTATE REVENUES			
Measure of Revenues	**LEC**	**IXC**	**Other**
Retail Revenues	47%	43%	10%
Revenues minus payments to other carriers	63%	25%	12%
UNIVERSAL SERVICE CONTRIBUTIONS BASED ON INTERSTATE REVENUES			
Retail Revenues	14%	81%	5%
Revenues minus payments to other carriers	40%	55%	5%

Thus, using NYNEX's figures, if the Commission uses only interstate revenues to apportion universal service support, 81% of the support will be provided by interexchange carriers and 14% by local exchange carriers. Clearly, using only interstate retail revenues to apportion universal service support among carriers would impose a disproportionate burden on interexchange carriers. In contrast, if the Commission uses revenues less payments made to other carriers local exchange carriers will bear between 40% (interstate) and 63% (interstate and intrastate) of the universal service burden depending on whether the Commission uses interstate or interstate and intrastate revenues.

The comments reveal four general options for determining universal service support:

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[48] NYNEX at pp. 19-20.